

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Ruth Y. Goldway, Chairman;
Mark Acton, Vice Chairman;
Nanci E. Langley; and
Robert G. Taub

Competitive Product Prices
Inbound Competitive Multi-Service Agreements
with Foreign Postal Operators
Australian Postal Corporation—United States Postal Service
Bilateral Agreement (MC2010-34)
Negotiated Service Agreement

Docket No. CP2012-1

ORDER CONCERNING AN ADDITIONAL INBOUND COMPETITIVE MULTI-SERVICE
AGREEMENTS WITH FOREIGN POSTAL OPERATORS 1
NEGOTIATED SERVICE AGREEMENT

(Issued November 9, 2011)

I. INTRODUCTION

The Postal Service requests to add a specific agreement to the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product established in Docket No. MC2010-34. For the reasons discussed below, the Commission approves the request.

II. BACKGROUND

On October 17, 2011, the Postal Service filed a notice, pursuant to 39 CFR 3015.5 and Order No. 546, that it has entered into an additional Inbound Competitive

Multi-Service Agreements with Foreign Postal Operators 1 agreement.¹ The Notice concerns the portion of a bilateral agreement with Australian Postal Corporation (Australia Post Agreement) for inbound competitive services that the Postal Service seeks to add to the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product.

In Order No. 546, the Commission approved the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product and the Koninklijke TNT Post BV and TNT Post Pakketservice Benelux BV (TNT Agreement). The Postal Service asserts that its filing demonstrates that the Australia Post Agreement fits within the Mail Classification Schedule (MCS) language in Governors' Decision No. 10-3 originally filed in Docket Nos. MC2010-34 and CP2010-95. Notice at 3-4. Additionally, it contends that the Australia Post Agreement is functionally equivalent to the agreement filed in Docket No. CP2010-95. *Id.* at 3. In Order No. 840, the Commission approved the functionally equivalent Norway Post Agreement and the designation of the TNT Agreement as the baseline agreement for purposes of functional equivalency analysis of the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product.²

The Postal Service also filed supporting materials including a redacted copy of the Australia Post Agreement, supporting financial documentation, and an application for non-public treatment of materials filed under seal.

The Australia Post Agreement covers, *inter alia*, the delivery of inbound Air Parcel Post (Air CP) and Express Mail Services (EMS). Notice at 3. The Postal Service's Notice states that the parties intend for the rates to become effective January

¹ Notice of United States Postal Service of Filing Functionally Equivalent Inbound Competitive Multi-Service Agreement with a Foreign Postal Operator, October 17, 2011 (Notice); *see also* Docket Nos. MC2010-34 and CP2010-95, Order Adding Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 to the Competitive Product List and Approving Included Agreement, September 29, 2010 (Order No. 546).

² See Docket No. CP2011-69, Order Concerning an Additional Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 Negotiated Service Agreement, September 7, 2011 (Order No. 840).

1, 2012, and to remain in effect for 2 years. *Id.* at 4, Attachment 1 at 1. The Australia Post Agreement may be terminated without cause with 30 days' notice. *Id.*, Attachment 1 at 6.

The Postal Service contends that the Australia Post Agreement to deliver inbound Air CP and EMS in the United States is functionally equivalent to the agreement to deliver inbound Air CP and EMS in the TNT Agreement. *Id.* at 3. The Postal Service asserts that the Australia Post Agreement is similar in both product and cost characteristics to the TNT Agreement. *Id.* at 5. It states that the TNT Agreement includes similar terms and conditions, *e.g.*, is an agreement with a foreign postal operator and conforms to a common description. *Id.* The Postal Service identifies differences that distinguish the instant agreement from the TNT Agreement, but asserts that these differences affect neither the fundamental service the Postal Service is offering nor the fundamental structure of the agreement. *Id.* at 5-7.

The Postal Service contends that the Australia Post Agreement and the TNT Agreement incorporate the same cost attributes and methodology, and the relevant cost and market characteristics. *Id.* at 7. Despite some differences, the Postal Service asserts that the Australia Post Agreement is functionally equivalent to the TNT Agreement previously filed. *Id.*

In its Notice, the Postal Service maintains that certain portions of the Australia Post Agreement, prices, and related financial information, should remain under seal. *Id.* at 4, Attachment 4.

The Postal Service concludes that the Australia Post Agreement complies with 39 U.S.C. 3633. *Id.* at 7. Therefore, it requests that the Commission add the Australia Post Agreement to the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product. *Id.* at 8.

In Order No. 919, the Commission gave notice of the docket, appointed a Public Representative, and provided the public with an opportunity to comment.³ On October 26, 2011, Chairman's Information Request No. 1 was issued that sought clarification of the rates used in the Postal Service's financial work papers filed under seal and any pay-for-performance arrangement applicable to inbound EMS and Air CP from Australia.⁴ The Postal Service responded to CHIR No. 1 on October 28, 2011, and filed a revised version of supporting financial documentation.⁵

III. COMMENTS

Comments were filed by the Public Representative.⁶ No other interested person submitted comments. The Public Representative reviewed the Australia Post Agreement's functional equivalence with the TNT Agreement in Docket No. CP2010-95 and compliance with 39 U.S.C. 3633(a). *Id.* at 2-5. He states that the Australia Post Agreement has specific differences as identified in the Postal Service's Notice that do not affect the fundamental service or structure of the agreements. He maintains that these differences include different foreign postal operators, customs inspection, terms and renewal, presorting and routing requirements and other changes. *Id.* at 3.

However, the Public Representative also maintains that the Postal Service's response to CHIR No. 1, question 3, indicates that inbound Air CP from Australia will not be subject to pay-for-performance requirements. *Id.* at 4. He paraphrases that the Postal Service's response to the question as indicating that "[f]or inbound Air CP from Australia, no pay-for-performance arrangements will apply." *Id.* at 3. He states, by

³ Notice and Order Concerning Filing of an Additional Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 Negotiated Service Agreement, October 21, 2011 (Order No. 919).

⁴ Chairman's Information Request No. 1, October 26, 2011 (CHIR No. 1).

⁵ United States Postal Service Response to Chairman's Information Request No. 1 and Notice of Filing Non-Public Materials, October 28, 2011 (Response to CHIR No. 1).

⁶ Public Representative Comments on Postal Service Notice of Filing an Additional Negotiated Service Agreement for Inclusion Within Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1, October 31, 2011 (PR Comments).

contrast, the TNT Agreement applies negotiated performance thresholds and penalties to both EMS and Air CP. As a result, he concludes the Australia Post Agreement and TNT Agreement are not sufficiently similar or functionally equivalent. *Id.* at 3-4.

The Public Representative does state that the revised financial model filed under seal in response to CHIR No. 1 indicates that the Australia Post Agreement should generate sufficient revenues to cover costs in conformity with 39 U.S.C. 3633(a). *Id.* at 4.⁷ However, he raises a concern about minimal cost coverage and notes that the Commission has raised similar concerns in its review of negotiated rates for EMS service in the FY2010 Annual Compliance Determination. *Id.*

The Public Representative also observes that the Australia Post Agreement applies the Kahala Post Group pay-for-performance criteria to inbound EMS from Australia, but the Postal Service's supporting documentation does not provide estimates on the effect of late delivery, late information, or missing information on revenues and cost coverage. *Id.* at 4-5. The Public Representative urges the Commission to obtain further information from the Postal Service regarding the projected performance of EMS and any potential effect on compliance with the requirements of 39 U.S.C. 3633. *Id.* at 5.

IV. COMMISSION ANALYSIS

The Postal Service proposes to add an additional agreement to the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product. First, the Commission reviews the agreement to ensure that it is functionally equivalent to the agreement approved in Docket No. CP2010-95, and thus belongs as part of the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product. Second, the Commission must ensure that the agreement at issue in this proceeding satisfies the requirements of rules 3015.5 and 3015.7, and 39 U.S.C. 3633.

⁷ The Public Representative also notes that the revised financial model filed in response to CHIR No. 1 indicates that the cost coverage is less than presented in the initial filing. Nevertheless, he acknowledges that the cost coverage does comply with section 3633.

Functional equivalence. The Postal Service states that the Australia Post Agreement shares similar cost and market characteristics with the TNT Agreement. It asserts that the instant contract meets the pricing formula and classification established in Governors' Decision No. 10-3, which comport with 39 U.S.C. 3633 and the Commission's rules. The Postal Service also identifies differences between the Australia Post Agreement and the TNT Agreement. These distinctions include different foreign postal operators, customs inspection, intellectual property, co-branding and licensing, rate table, and other differences. Notice at 5-7.

The Public Representative agrees that certain changes, as noted above, do not affect functional equivalence. PR Comments at 3. However, as also noted above, he maintains that the Australia Post Agreement does not appear to include pay-for-performance requirements for inbound Air CP. *Id.* In response to CHIR No. 1, question 3, the Postal Service states, "[n]o other pay for performance arrangement will apply to inbound air parcels from Australia." The Commission interprets the word "other" to mean that the Universal Postal Union (UPU) pay-for-performance arrangements do apply. Annex 1 of the Australia Post Agreement also indicates that the rates for inbound Air Parcels incorporate a provisional quality link performance, which may potentially be adjusted depending on performance results in accordance with current UPU rules.⁸ Therefore, it appears that the terms for Air CP in the Australia Post Agreement are similar to the terms for Air CP in the TNT Agreement.

The instant agreement therefore appears to be similar to the agreement filed in Docket No. CP2010-95, although it differs in some minor respects relative to certain general terms. These differences notwithstanding, the Commission concludes that the instant agreement is functionally equivalent and may be included in the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product.

⁸ Annex 1 of the Australia Post Agreement notes that the rates incorporate provisional quality link performance, which may be adjusted based on performance results in accordance with current UPU rules.

Compliance with 39 U.S.C. 3633. The Commission reviews competitive products to ensure that they meet the applicable requirements of rules 3015.5 and 3015.7, and 39 U.S.C. 3633. The Public Representative is concerned that the instant agreement's compliance with section 3633 may be impacted by pay-for-performance requirements or cost and revenue estimates associated with its negotiated rates. *Id.* at 4-5. As acknowledged by the Public Representative, the instant Agreement meets the requirements of section 3633. The Commission's view is that there is no need to take additional action at this time. Because any pay-for-performance bonuses received by the Postal Service for Air Parcels will increase revenues, the rates should cover attributable costs. In any event, the Commission will have the opportunity to assess the Postal Service's performance under the instant agreement in future annual compliance determinations.

The Commission has also carefully considered the Public Representative's concern that the Postal Service's supporting documentation does not provide estimates of the effect of late delivery, late information, or missing information on revenues and cost coverage for inbound EMS. Under the Australia Post Agreement, the Kahala Post Group's pay-for-performance criteria apply. Worksheets 9 and 10 filed on October 17, 2011 in the nonpublic financial documentation include the pay-for-performance thresholds and penalties, as well as the Postal Service's historic and projected performance. The Commission further reviewed the Postal Service's most recent EMS service performance based on its UPU EMS Cooperative report cards, and considers the Postal Service's risk of incurring financial penalties to be minimal. Therefore, estimates of the effect of late delivery, late information, or missing information on revenue and cost coverage for inbound EMS are not necessary.

The Commission has reviewed the Notice, financial analyses provided under seal that accompanies the instant contract, responses to CHIR No. 1, as well as the comments filed in this proceeding. Based on the information provided, the Commission finds that the agreement submitted should cover its attributable costs (39 U.S.C. 3633(a)(2)), should not lead to the subsidization of competitive products by market

dominant products (39 U.S.C. 3633(a)(1)), and should have a positive effect on competitive products' contribution to institutional costs (39 U.S.C. 3633(a)(3)). Thus, a preliminary review of the instant agreement indicates that it comports with the provisions applicable to rates for competitive products.

Other considerations. The Postal Service states that the parties intend for January 1, 2012 to be the effective date of the Australia Post Agreement. If this date changes, the Postal Service shall notify the Commission of the effective date. The Postal Service shall promptly notify the Commission if the Australia Post Agreement terminates earlier than its proposed term, but no later than the actual termination date.

In addition, within 30 days of expiration, or early termination of the Australia Post Agreement, the Postal Service shall file costs, volumes, and revenues data associated with the Australia Post Agreement.

In conclusion, the Commission finds that the Australia Post Agreement submitted in Docket No. CP2012-1 is appropriately included within the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product.

V. ORDERING PARAGRAPHS

It is ordered:

1. The Australia Post Agreement filed in Docket No. CP2012-1 is included within the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 (MC2010-34) product.
2. The Postal Service shall notify the Commission of the effective date of the Australia Post Agreement and update the Commission if the Agreement terminates prior to the scheduled termination date as discussed in this Order.

3. Within 30 days of expiration, or upon early termination of the Australia Post Agreement, the Postal Service shall file costs, volumes, and revenues data associated with the agreement.

By the Commission.

Shoshana M. Grove
Secretary